UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF INDIANA
HAMMOND DIVISION

IN RE:	)	
	)	
SANDRA A. PRICE,	)	CASE NO. 05-68006
	)	Chapter 7
Debtor.	)	
**********		
REGENCY HOSPITAL OF NORTHWEST INDIANA, L.L.C.,	)	
	)	
Plaintiff,	)	
v.	)	ADVERSARY NO. 05-6181
	)	
SANDRA A. PRICE,	)	
	)	
Defendant.	)	

MEMORANDUM OF DECISION AND ORDER ON
PLAINTIFF'S MOTION FOR SUMMARY JUDGMENT

This matter comes before the Court on the motion for summary judgment of the Plaintiff, Regency Hospital of Northwest Indiana, L.L.C. ("Regency"). Regency asserts that the debt owed by the Defendant, Sandra Price ("Price"), should be excepted from discharge pursuant to 11 U.S.C. § 523(a)(4) and § 523(a)(6) of the United States Bankruptcy Code ("Code"); Price of course disputes that assertion. This Court has jurisdiction over this adversary proceeding pursuant to 28 U.S.C. § 1334(b), 28 U.S.C. § 157(a), and N.D.Ind.L.B.R. 200.1(a)(2). This matter constitutes a "core" proceeding as defined by 28 U.S.C. § 157(b)(2)(I).

I. Statement of the Case

Sandra Price filed a petition for relief under Chapter 7 of the United States Bankruptcy Code on March 31, 2005. On November 15, 2005, Regency initiated this adversary proceeding against Price, alleging that indebtedness owed by Price to Regency is excepted from discharge pursuant to 11 U.S.C. §523(a)(4) and (a)(6). Price, by counsel, filed an answer and affirmative defenses on June 21, 2006, which denied the substantive averments of Regency's complaint. On December 6, 2005, Regency filed a motion for summary judgment, together with a

supporting memorandum and a designation of materials it deemed to constitute the record necessary for its motion. On March 24, 2006, this Court entered a briefing schedule for purposes of summary judgment, and with various extensions of time, briefing in this matter closed on August 3, 2006.

Regency's summary judgment motion is based upon the principles of collateral estoppel. On November 9, 2004, Regency sued Price, and other named defendants, in the Lake County Superior Court under cause number 45D04-0411-PL-00054, by means of a complaint which requested damages, pre-judgment attachment, pre-judgment garnishment and injunctive relief.[1] On November 22, 2004, an Amended Complaint was filed which, in addition to the above, included the allegation that Price converted approximately $302,086.63 of the creditor's funds, in contravention of I.C. 34-24-3-1, and included claims for breach of contract, suit on account, and to set aside and recover certain fraudulent conveyances.[2] On July 6, 2005, this matter went to trial in the state court and a judgment in the amount of $403,047.67 was entered against Price. The judgment included actual damages in the amount of $302,086.63, plus interest from October 26, 2004 at eight percent per annum, and attorneys' fees and costs in the amount of $50,961.04. Additionally, the court found that the Plaintiff, pursuant to I.C. 34-24-3-1, was entitled to treble damages, and thereby increased the award by $50,000 for a total of $403,047.67. The judgment provided that Regency was to give credit to Price for funds recovered from several sources. Regency asserts that the facts and issues determined in this state court case are fact and issue preclusive in this adversary proceeding.

This matter is now before the Court to enter a decision on the Plaintiff's Motion for

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[1] Upon a motion for change of judge brought by the Defendant, this matter was reassigned to a special judge and then proceeded under cause number 45D11-0503-PL-18.

[2] The additional defendants named to the state court action were the alleged recipients of certain purported fraudulent transfers.

Summary Judgment.

II. Standards for Review of Motions for Summary Judgment

The procedural mechanism of summary judgment is provided by Rule 56 of the Federal Rules of Civil Procedure, made applicable to adversary proceedings by Fed.R.Bankr.P. 7056. The principle standard to be followed by the Court in determining a motion for summary judgment is stated as follows in Fed.R.Civ.P. 56(c):

> The judgment sought shall be rendered forthwith if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law.

The inquiry that the court must make is whether the evidence presents a sufficient disagreement to require trial or whether one party must prevail as a matter of law. *Anderson v. Liberty Lobby*, 106 S. Ct. 2505, 2509-10 (1986). In deciding a Motion for Summary Judgment, the Court should not "weigh the evidence." *Anderson*, 477 U.S. at 249, 106 S. Ct. at 2510-11; *Illinois Bell Telephone Co. v. Haines and Co., Inc.*, 905 F.2d 1081, 1087 (7th Cir. 1990). However, "if evidence opposing a summary judgment is merely colorable, or is not significantly probative, summary judgment may be granted." *Anderson*, 106 S. Ct. at 2511; *Trautvetter v. Quick*, 916 F.2d 1140, 1147 (7th Cir. 1990).

The moving party bears the burden of showing that there is an absence of evidence to support the non-movant's case; *Celotex Corp. v. Catrett*, 106 S. Ct. at 2548, 2554 (1986), i.e., the lack of a genuine issue of material fact. *Big O Tire Dealers, Inc. v. Big O Warehouse*, 741 F.2d 160, 163 (7th Cir. 1984); *Korf v. Ball State University*, 726 F.2d 1222, 1226 (7th Cir. 1984).

When ruling on a motion for summary judgment, inferences to be drawn from underlying facts contained in such materials as attached exhibits and depositions must be viewed in a light most favorable to the party opposing the motion. *United States v. Diebold, Inc.*, 82 S. Ct.

993, 994 (1962); *See also, Matsushita Elec. Indus. Co. Ltd. v. Zenith Radio Corp.*, 106 S. Ct. 1348, 1356, (1986) (All inferences to be drawn from the underlying facts must be viewed in a light most favorable to the nonmoving party); *Yorger v. Pittsburgh Corning Corp.*, 733 F.2d 1215, 1218 (7th Cir. 1984); *Marine Bank Nat. Ass'n. v. Meat Counter, Inc.*, 826 F.2d 1577, 1579 (7th Cir. 1987). Fed.R.Civ.P. 56(e) requires the nonmoving party to set forth specific facts, which demonstrate that genuine issues of fact remain for trial. *Matsushita Elec. Indus. Co., Ltd. v. Zenith Radio Corp.*, 106 S. Ct. at 1355; the opposing party may not defeat the motion by merely relying on the allegations or denials in its pleadings.

The ultimate burden of proof at the trial of this Adversary Proceeding is on the party seeking an exception to discharge, and that party bears the burden of proof as to each element. *Matter of Scarlata*, 979 F.2d 521, 524 (7th Cir. 1992); *In re Kreps*, 700 F.2d 372, 376 (7th Cir. 1987). *See also, In re Martin*, 698 F.2d 883, 887 (7th Cir. 1983), (§ 727 general discharge). In bankruptcy, exceptions to discharge are to be construed strictly against a creditor and liberally in favor of the Debtor. *In re Scarlata*, 979 F.2d at 524, *supra, quoting, In re Zarzynski*, 771 F.2d 304, 306 (7th Cir. 1985).

As to the standard of proof, it should be noted that the Supreme Court in the case of *Anderson, et. al. v. Liberty Lobby, Inc. and Willis A. Carto*, 106 S. Ct. 2505 (1986) held that in determining whether a factual dispute exists on a motion for summary judgment, the court must be guided by the substantive evidentiary standards of the case that are applicable at trial. The standard of proof in a § 523(a) nondischargeability adversary proceeding is by a preponderance of evidence, rather than the more stringent standard of clear and convincing evidence. *See, Grogan v. Garner*, 111 S. Ct. 654 (1991).

III. Materials to be Considered by the Court

F.R.C.P. Rule 56(c) provides that the Court is to consider "the pleadings, depositions,

answers to interrogatories, and admissions on file, together with the affidavits, if any," in determining whether or not a genuine issue/genuine issues of material fact exist. N.D.Ind.L.B.R. B-7056-1 sets forth certain procedural requirements which must be met to properly present a motion for summary judgment to the Court for decision. The purpose of N.D.Ind.L.B.R. B-7056-1 is to provide a clear record of the material facts upon which Rule 56's application depends, so that the Court does not need to overturn rocks and look behind trees in order to determine the dispositive facts the parties are relying on for purposes of summary judgment and where those facts are in the record. Principal among the requirements of that rule is the submission by the proponent of a "Statement of Material Facts." Unfortunately, more often than not, this Statement is done incorrectly. Almost without exception, the response of the opponent of the motion to the proponent's Statement – which the local rule denominates as the "Statement of Genuine Issues" – is done totally incorrectly. So it has transpired in this case.

In this case, Regency filed a separate document entitled "Designation of Evidence for Purposes of Summary Judgment", to which are attached certain documentary materials. Regency then included a section in its brief entitled "Statement of the Facts", which raises the question: Is this just a rendition of the facts of the case, or are these the material facts the Court is to review to determine the motion? The rule contemplates a single – just one – recitation of material facts, which may be incorporated into the supporting initial brief (in which case the documentary material would be attached as exhibits to the brief), or filed as a separate document (in which case the brief would not contain a separate recitation of material facts). Given that Regency's Statement of Facts in its brief directly cites to evidence contained in the Designation, the Court will consider the Statement of Facts in the brief to be the material facts Regency is relying on for summary judgment, and the Designation to be in nature of an exhibit

appendix. The appendix contains a certified copy of the state court judgment and an affidavit as to its authenticity.

Price's counsel's response demonstrates why the Court DESPISES summary judgment motions, and why the Court seeks to limit their use. Instead of the "Statement of Genuine Issues" required by N.D.Ind.L.B.R. B-7056-1, Price has submitted a bunch of exhibits under the designation "Defendant's Exhibits", and a section in the response memorandum entitled "Material Facts About Which There is a Genuine Issue". This latter testament doesn't contain fact one; rather, it is a set of five numbered questions, devoid of reference to the record. It is essentially a statement of issues to be determined from the facts – not a statement of the facts themselves. Properly done, a "Statement of Genuine Issues" is a recitation of FACTS – cited to the record as supported by materials properly introduced into the summary judgment record – which the opponent of the motion asserts are contrary to the facts stated by the proponent in its "Statement of Material Facts". Price's submission entirely fails to conform to the requirements of N.D.Ind.L.B.R. B-7056-1, and the Court will not consider any facts stated in Price's response on the matter before it. This is not prejudicial to Price, however, in that the pertinent facts are all contained in the state court judgment. Even if the Court were to consider the materials submitted by Price's counsel, they are all irrelevant, dealing as they do with matters which preceded the trial in the state court and the final judgment entered by that court.[3]

The facts established of record for the purposes of Regency's motion for summary judgment are the following:

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[3] As is true with much of the argument advanced by Price in opposition to the motion for summary judgment, the alleged "factual" materials submitted by Price essentially seek to argue the unfairness of the state court's procedures, a matter which should have been the subject of an appeal in the state system if Price believed the procedures to have been legally defective. The issues of collateral estoppel before the Court depend solely upon the FINAL judgment of the state court rendered following its trial on the merits.

1. Judge Jeffery Dywan, Special Judge, in Case Number 45D11-0503-PL-18 in the Lake Superior Court, Room Seven, in Crown Point, Indiana, held a bench trial on July 6, 2005. Price was fully represented by counsel at that trial.

2. On August 29, 2005, Judge Dywan entered his "Findings and Judgment" which was a final judgment disposing of all the issues in the case. A true, accurate, and certified copy of the Findings and Judgment is attached as Exhibit B to Regency's Non-Dischargeability Complaint.

3. Price took no appeal from the final judgment entered by Judge Dywan, and the time for taking such an appeal to a higher court has expired.

4. The judgment of the Lake Superior Court provided in pertinent part as follows [the most pertinent portions are bolded]:

> **FINDINGS AND JUDGMENT**
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> This cause came before the Court for trial, without the intervention of a jury, on July 6, 2005. The Plaintiff Regency Hospital Company of Northwest Indiana, LLC, was present in court through Bobby Franklin, one of its representatives. Plaintiff was represented by Robert F. Peters of the firm of Lucas, Holcomb & Medrea, LLP. The Defendant Sandra A. Price was present, in person, for trial and all of the Defendants were represented at trial by Richard Gordon Hatcher of Hatcher & Associates. The Defendant Robert Brandy was present in court, but did not testify. The other Defendants were not present for trial. The plaintiff and the defendants have filed written arguments and proposed findings and judgments. Although neither Plaintiff nor Defendants requested special findings of fact, the Court, on its own motion, makes findings of fact with regard to some of the relevant issues for purposes of rendering judgment in this case.
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> **Findings of Fact**
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> After hearing all of the evidence in this cause, including the depositions of Wiley Gene Winters and Torena Grable, and further including the certified transcripts of evidence and exhibits received in the hearings held by the Court on November 22, 2004, December 1, 2004, and December 9, 2004, the Court finds the following facts in support of its judgment herein:
> **On April 30, 2004, Sandra A. Price arranged to have her**

husband, Clarence W. Price, admitted to Regency Hospital of Northwest Indiana, LLC (hereafter "Regency"), an urgent extended care medical facility. Mr. Price was in very poor health and his condition did not permit him to consent to his own medical treatment. Sandra Price, therefore, completed the forms necessary for his admission. One of the forms that Regency requested her to sign was a form entitled "Conditions of Admission to Regency Hospital". This form provided consent to hospital care for Mr. Price and further provided as follows:

> **6. Assignment of Insurance Benefits: In the event the undersigned is entitled to hospital benefits of any type whatsoever arising out of any policy of insurance insuring patient or any other party liable to patient, said benefits are hereby assigned to Regency Hospital for application on patient's bill, and it is agreed that the hospital may receipt for any such payment and such payment shall discharge the said insurance company of any and all obligations under the policy to the extent of such payment, the undersigned and/or patient being responsible for charges not covered by this assignment.**
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> **7. Financial and Payment Guarantee: Both undersigned patient and guarantor(s) agree that in consideration of the services to be rendered to the patient, they hereby individually obligate themselves to pay the charges of the hospital in accordance with the regular rates and terms of Regency Hospital. Should the account be referred to an attorney for collection, the undersigned shall pay reasonable attorney's fees and collection expenses. All delinquent accounts bear interest at the legal rate.**

The Court finds that Regency requested Sandra Price to approve of the conditions of admission, that she did in fact approve of the conditions of admission, and that Regency Hospital justifiably relied upon the terms and provisions set forth in subsequently rendering medical care to Clarence Price. **The Court finds that Sandra Price signed her husband's name as the patient on the bottom of the form, showed her relationship as his spouse, and then signed the form herself where it provides a space for the patients signature. She intended to approve the form and to provide the necessary consent for Regency to give medical care to her husband.**

Regency obtained information from Mrs. Price that she and her husband were insured with Anthem Blue Cross Blue Shield (hereafter "Anthem"), a medical insurance policy that was in her name which she had by reason of her employment. Regency provided medical services to Clarence Price that were similar to what would be provided in the context of a hospital intensive care unit. Treatment was provided to Clarence Price from April 30, 2004, until July 18, 2004, at which time he was discharged.

Following its standard practice, Regency sent a bill to Anthem for the services rendered to Mr. Price in the sum of $303,236.63. Anthem reviewed the billing, approved it, and on or about October 4, 2004, issued a benefit check for payment on the medical expenses in the sum of $302,086.63, which check was made payable to Sandra Price and forwarded directly to her. At the same time, Anthem provided an explanation of benefits form to Sandra Price advising that, before payment, she owed Regency Hospital $303,236.63 and that Anthem was issuing a check paying $302,086.63 of this amount on the Regency claim. Regency Hospital had previously notified Sandra Price that the Anthem payment check for Regency's services would be made payable to her and sent directly to her. They advised her of the amount of the check and she reacted with surprise. Regency requested that she immediately endorse and bring in the check to Regency Hospital to apply on the bill and Mrs. Price indicated that she would do so as soon as she received it. Numerous phone calls were placed by a Regency representative to Mrs. Price, but most of them were unanswered and there was no return call for the messages left by Regency. Torena Gable of Regency sent correspondence to Clarence Price by certified mail, return receipt requested, reminding him that the conditions for admission form contained an assignment of insurance benefits to Regency Hospital. Sandra Price received the letter and signed the return receipt. Unbeknownst to Regency Hospital at that time, Clarence Price had died after his discharge from Regency.

After she received the check, Sandra Price consulted with Attorney George Paras and advised him that she had signed a form containing an assignment of insurance benefits to Regency and that she had a check from Anthem payable to her in the sum of $302,086.63. Attorney Paras advised her that, since she had approved the assignment of benefits language, Regency was entitled to all of the money that had been paid by Anthem. Nevertheless, Sandra Price negotiated the benefit check in the sum of $302,086.63 at Centier Bank

on or about October 19, 2004. Thereafter, on or about October 26, 2004, Sandra Price used the funds in question to purchase at least 23 separate official bank check payable primarily to relatives who resided in Indiana, Illinois, Wisconsin and Minnesota. A substantial majority of the checks were each made payable in the sum of $5,000.00, with a few of them being for lesser amounts. Using the Anthem funds, Sandra Price made checks payable to each of the Defendants named in the Plaintiff's Amended Complaint herein.

Not all those receiving checks from Sandra Price have been named in this case. Many of them live in other states. The Court finds that each of the following individuals received the following checks from the funds in question:

(Chart Omitted)

Counsel for Plaintiff advised the Court that although two $5,000.00 bank checks were each made payable to Ronald and Ricky Bandy, said Defendants did not negotiate the checks and, by reason of the stop payment order issued by the Court in this cause, the funds represented by the checks to said Defendants totaling $10,000.00 was paid into the Clerk of the Court by Centier Bank. Plaintiff is therefore not requesting any personal judgment against Ronald Bandy and Ricky Bandy, but is only requesting that the funds paid into the Clerk of the Court be applied on any judgment rendered in favor of Regency in this case.

In addition to making the foregoing disbursements, Sandra Price, using the Anthem funds, purchase a new four-door 2005 Chrysler 300 automobile, model CA63, Indiana license plate no. 45Q2014, VIN 2C3AA63H55H521504. Said vehicle, by reason of prior orders entered by this Court, has been attached and is presently held in storage by Plaintiff pending the outcome of this case.

. . .

Upon obtaining the funds assigned to Regency, Sandra Price paid non-medical bills that she owed, bought new furniture and carpeting for her apartment, and gave additional portions of the funds to her co-workers at the Lake County office of the Division of Family and Children.

The Court finds that all of the transfers of funds to the Defendants and other friends of Sandra Price were made gratuitously, without consideration being exchanged, and that the transfers were made by Sandra Price with the specific intention of hindering payment, defrauding Regency,

or otherwise making the funds unavailable to Regency for the payment on the account of Clarence Price. Following the expenditures made by Sandra Price and the fraudulent transfers to the Defendants and others, Sandra Price has no funds remaining in order to pay the bill in question to Regency, other than the funds that have been frozen by Regency and have been paid into the Clerk of this Court. Sandra Price has not paid anything to Regency on account of the services rendered to her husband and she further did not use the Anthem funds to pay any other medical bills pertaining to her husband. By making the transfers in question, Sandra Price has deliberately rendered herself judgment-proof so that there would be few, if any, funds available to pay Regency.

The Court finds that, in addition to the foregoing, Sandra Price caused four separate bank checks to be made payable to herself, each in the sum of $25,000.00 and at least two other bank checks from said funds being made payable to her in the sum of $5,000.00 each. Sandra Price has testified that none of these funds remain available to be paid on the Regency bill.

The Court finds that, using the funds in question from Anthem, Sandra Price opened an individual account at Centier Bank, checking Account No. 11164105, which had remaining $17,104.81 in it. She further used the funds in question to open a joint checking account, Account No. 11168218, in the names of Sandra A. Price and Robert Bandy (her brother) which had $34,133.70 remaining in it. Pursuant to prior orders of this Court, the money remaining in each of the foregoing accounts was paid into the Clerk of the Court to be held subject to the Court's judgment herein. In addition to the foregoing, Centier Bank has, pursuant to the prior orders of this Court, paid into the Clerk's Office the sum of $10,000.0 (checks not negotiated by Ricky Bandy and Ronald Bandy), and sum of $5,000.00 which was in the account of Defendant Willa M. Crozier, together with her husband, Wilbur Crozier. These funds represent money that Sandra Price gave to Willa Crozier out of the Anthem Funds. There was also an additional $12.11 paid into the Clerk of the Court by Centier Bank out of another checking account in the name of Sandra Price, Account No. 11164105.

The Court finds that, at all times in question, Sandra Price intentionally acted dishonestly with the intent to exercise unauthorized control over the funds paid by Anthem which

belonged to and were the property of Regency by reason of the assignment of benefits provision approved by her. The Court finds that the medical services rendered to Clarence Price were necessary and that the charges made by Regency Hospital in its billing were reasonable and based on a market study in Northwest Indiana.

The Court finds that Clarence Price left little or no assets which are available to pay the Regency claim and Sandra Price, by reason of her employment, her Anthem policy, and subsequent receipt of the check from Anthem, had the superior ability to pay Regency for the necessary care that was being rendered to her husband at her request. The Court finds that Sandra Price is liable under the doctrine of necessaries for the Regency bill and she should be estopped from denying that she approved the assignment of benefits language. Allowing Sandra Price to keep the funds that Anthem paid by reason of the Regency claim would constitute unjust enrichment to her.

The Court finds that by reason of the unlawful conversion of funds belonging to Regency and the failure of Sandra Price to pay the Regency bill, Regency has incurred reasonable attorney's fees prior to trial, in the sum of $43,610.75, plus an additional $4,850.29 in costs, for a total of $48,461.04. In addition, the Court finds that the further sum of $2,500.00 in reasonable attorney's fees has been incurred for the services of Plaintiff's counsel in the trial of this case, the preparation of closing arguments, and in the preparation of a proposed judgment with findings which was prepared at the request of the Court. The Court finds that Regency is entitled to recover attorney's fees against Sandra Price on two separate bases. First, by reason of paragraph 7 of the Conditions of Admission; and second, by reason of her conversion of the funds which were paid by Anthem and were subject to the assignment of benefits language in the Conditions of Admission.

The Court finds that Sandra Price approved the assignment of benefits language in the Conditions of Admission and that said provisions are binding upon her, notwithstanding the manner in which she executed the agreement. The Court finds that there was no condition placed on the agreement which indicated that Sandra Price would be bound personally only if she signed the form and she, through her acts and conduct, consented to and approved of the provisions in the Conditions of Admission. That Court finds that the assignment of benefits to Regency is further upheld under the doctrine of equitable assignment, and that after approving the assignment of benefits, Sandra Price had no right,

> title or interest in the Anthem proceeds in question notwithstanding the fact that the check was made payable to her, and she held said funds in trust solely for the benefit of Regency and was obligated to promptly pay said funds to Regency.
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> See, *Findings and Judgment,* pgs. 1-9.

IV. Analysis

The gravamen of Regency's motion is that the findings of fact and judgment entered by the state court establish that the indebtedness determined by the state court is excepted from discharge under 11 U.S.C. § 523(a)(4) and § 523(a)(6). Therefore, the Court's analysis will essentially be a determination of whether the facts and issues adjudicated by the state court rise to the level of dischargeability as pled in the complaint.

In an adversary proceeding to determine the non-dischargeability of a debt, the burden of proof is on the plaintiff as to each element of the statutory exception to discharge; *In re Kreps*, 700 F.2d 372, 376 (7th Cir. 1983); *Zygulski v. Daugherty*, 236 B.R. 646, 653 (Bankr. N.D.Ind. 1999), citing, *Matter of Scarlata*, 979 F.2d 521, 524 (7th Cir. 1992). Furthermore, exceptions to discharge are to be construed strictly against the creditor and liberally in favor of the debtor; *Matter of Scarlata*, 979 F.2d at 524 (citing, *In re Zarzynski,* 771 F.2d 304, 306 (7th Cir. 1985)). The United States Supreme Court has held that the standard of proof in nondischargeability proceedings under § 523(a) is a preponderance of evidence standard rather than the more stringent standard of clear and convincing evidence; *Grogan v. Garner*, 498 U.S. 279 (1991).

Regency asserts that the facts and issues already determined by the state court's decision give rise to collateral estoppel with respect to its complaint in this adversary proceeding. It is undisputed that collateral estoppel applies in the bankruptcy context; *In re Jones*, 180 B.R. 531, 532 (Bankr. S.D.Ind. 1994) citing *Grogan V. Garner*, 498 U.S. 279. n. 11, 111 S.Ct. 654, 658, n.11, 112 L.E.2d 755 (1991). A state court judgment is entitled to full faith and credit in bankruptcy proceedings; 28 U.S.C. § 1738 (West 2006); *Matter of Bulic*, 997 F.2d

299, 304 (7th Cir. 1993). The effect of a judgment in subsequent litigation is determined by the law of the jurisdiction that rendered the judgment. *In re Catt*, 368 F.3d 789, 790-91 (7th Cir. 2004); *Wolverine Mutual Insurance v. Vance*, 325 F.3d 939 (7th Cir. 2003); *In re Scarborough*, 171 F.3d 638 (8th Cir. 1999) *cert. denied* 528 U.S. 931 (1999); *In re Keaty*, 397 F.3d 264, 270 (5th Cir. 2005) (discussing the requirement of "actually litigated"); *Brokaw v. Weaver*, 305 F.3d 660, 669 (7th Cir.2002) ["The preclusive effect of a state court judgment in a federal case is a matter of state rather than of federal law"]. Thus, the effect of the Lake Superior Court judgment for collateral estoppel purposes is governed by Indiana law.

Collateral estoppel bars the resuscitation of factual and legal issues that have been previously litigated and finally determined. Under Indiana law, the elements for the application of collateral estoppel are the following: (1) the issue sought to be precluded is the same as that involved in a prior action, (2) the issue was actually litigated, (3) determination of the issue was essential to the final judgment, and (4) the party to be estopped was fully represented in the prior action; *In re Jones*, 180 B.R. 531, 533 n.3 (Bankr. S.D.Ind. 1994); see also *Millenium Club, Inc. v. Avila*, 809 N.E.2d 906 (Ind. Ct. App. 2004) citing *Pritchett v. Heil*, 756 N.E.2d 561 (Ind. Ct. App. 2001); *Infectious Disease of Indianapolis, P.S.C. v. Toney*, 813 N.E.2d 1223, (Ind. Ct. App. 2004); *Tofany v. NBS Imaging Systems, Inc.,* 616 N.E.2d 1034 (Ind. 1993).[4] As stated in *Segovia v. State of Indiana*, 666 N.E.2d 105, 107 (Ind. App. 1996):

> In order to apply the doctrine of collateral estoppel, the court must engage in a two step analysis: "(1) determine what the first judgment decided; and (2) examine how that determination bears on the second case." *Webb v. State*, 453 N.E.2d 180, 183 (Ind. 1983), *reh. denied, cert. denied*, 465 U.S. 1081, 79 L. Ed. 2d 767, 104 S. Ct. 1449 (1984) (citing *United States v. Mespoulede*, 597

[4] Collateral estoppel applies under federal law under the same criteria; *Levinson v. United States*, 969 F.2d 260, 264 (7th Cir.1992) (citing *Klingman v. Levinson*, 831 F.2d 1292, 1295 (7th Cir.1987); *In re Massey*, 228 B.R. 686, 690 (Bankr. S.D.Ind. 1998); *In re Busick*, 264 B.R. 518, 522 (Bankr. N.D.Ind. 2001); *In re Staggs*, 177 B.R. 92, 95 (Bankr. N.D.Ind. 1995); In *re Lehman's Inc. of Andersen*, 163 B.R. 814, 816 (Bankr. S.D.Ind. 1994).

F.2d 329 (2d Cir. 1979)).

In addition, in the situation where a different claim is asserted in a subsequent lawsuit, collateral estoppel will still apply if an issue of fact material to both actions was determined in the prior case.[5] As stated in *In re Staggs*, 178 B.R. 767, 773 (Bankr. N.D.Ind. 1994) [citing the Restatement (Second) of Judgments]:

> When an issue of fact or law is actually litigated and determined by a valid and final judgment, and the determination is essential to the judgment, the determination is conclusive in a subsequent action between the parties, whether on the same or a different claim . . . A review of Indiana case law shows that this general rule is followed by the Indiana courts as well. *Bulic*, 997 F.2d at 304 n. 6 (quoting *Bicknell*, 118 Bankr. at 664 (citing *Hardesty v. Bolerjack*, 441 N.E.2d 243, 245 (Ind. App. 1982)).

In determining whether or not collateral estoppel applies in a subsequent proceeding, the court must examine the entire record before the court which entered the prior decision. Although arising in the context of a jury determination, as stated in *Segovia*, *supra*., 666 N.E.2d at 107:

> Determining what the first judgment decided involves an examination of the record of the prior proceedings including the pleadings, evidence, charge and any other relevant matters. 453 N.E.2d at 184. The court must then decide whether a reasonable jury could have based its verdict upon any factor other than the factor of which the defendant seeks to foreclose consideration. *Id*. If the jury could have based its decision on another factor, then collateral estoppel does not bar relitigation. *Id*.

As the state court has already entered a judgment, and made certain findings against the defendant under Indiana law – this Court must now determine whether or not the facts and issues decided rise to the level required for the debt to be excepted from discharge pursuant to 11 U.S.C. § 523(a)(4) and 11 U.S.C. § 523(a)(6).

A. 11 U.S.C. § 523(a)(4)

[5] This is certainly relevant in the matter before the Court now – in the state court action the plaintiff brought an action based on, among other things, the tort of conversion and to recover certain fraudulent transfers, and now brings a different claim before the bankruptcy court for dischargeability.

11 U.S.C. § 523(a)(4) provides that a debt is excepted from discharge if the debt is "for fraud or defalcation while acting in a fiduciary capacity, embezzlement, or larceny". In its Amended Complaint, Regency alleges that its debt, including the award of attorneys' fees and exemplary damages, is excepted from discharge under § 523(a)(4). In its brief, Regency argues that the debt should be excepted from discharge under § 523(a)(4) for two reasons – defalcation while acting in a fiduciary capacity, and for embezzlement.[6]

1. Defalcation while Acting in a Fiduciary Capacity

A critical component of a fiduciary relationship within the scope of 11 U.S.C. § 523(a)(4) is a *res* which exists as the focus of the relationship, much as would be the circumstance in the case of an express trust created to manage property deposited into the trust at the inception of the fiduciary relationship; *In re Tsikouris*, 340 B.R. 604 (Bankr. N.D.Ind. 2005). A mere promise to pay a debt when circumstances giving rise to the obligation to pay come into existence, made by an individual to another person or entity of equal or superior standing, is not within the ambit of 11 U.S.C. § 523(a)(4); *In re Woldman*, 92 F.3d 546 (7th Cir. 1996). Even if a contract, a statute, or an ordinance labels a relationship to be a "fiduciary" relationship, that label has no consequence under § 523(a)(4) unless there is an existing *res* which is mandated by law to be the subject of the labeled relationship; *In re McGee*, 353 F.3d 537 (7th Cir. 2003) [holding that a municipal ordinance which required the deposit of security deposits paid by tenants to a landlord into a segregated account, created a "fiduciary" relationship under 11 U.S.C. § 523(a)(4)].

In *Marchiando v. State of Illinois, Department of the Lottery*, 13 F.3d 1111 (7th Cir. 1994), the debtor was a licensed lottery agent for the State of Illinois, and under the contractual

[6] Though not artfully pled in its complaint and apparently not fully understood by the Defendant; under § 523(a)(4) embezzlement is embezzlement – there is no need to establish that a prior fiduciary relationship existed.

provisions of her arrangement with the state and by statute was deemed to be a "fiduciary" with respect to the State of Illinois for monies she received from the sale of Illinois lottery tickets. She failed to remit the proceeds of certain of those sales to the State of Illinois; when she filed bankruptcy, the state sought to except her liability to it for turnover of the sales proceeds from discharge under 11 U.S.C. § 523(a)(4). The United States Court of Appeals for the Seventh Circuit addressed the concept of "fiduciary capacity" as follows:

> Bankruptcy is both a creditor's remedy and a debtor's right. The discharge of the bankrupt's debts is an essential feature of the second function; it is what enables the bankrupt to get a "fresh start." It is also, depending on the bankrupt's future income prospects, a potentially great harm to creditors. When the bankrupt is a trustee and the creditor a beneficiary of the trust, the balance has been deemed to incline against discharge. Nondischarge becomes another token of the law's imposition of the highest standard of loyalty and care on trustees. In a trust relationship the settlor and beneficiary repose "trust" in a literal sense in the trustee, and the abuse of that trust is considered a serious wrong.
>
> The high standard of loyalty and care that the law imposes on trustees is encapsulated in the term "fiduciary duty." Once it entered the law's bank of concepts, it became available for use in situations that, while not involving trusts in a formal sense, seemed to call for the imposition of the same high standard. *Restatement (Second) of Trusts* § 2, comment b (1959). So a lawyer is deemed the fiduciary of his client, even if he does not manage a fund entrusted to him by the client, *Maksym v. Loesch,* 937 F.2d 1237, 1241-42 (7th Cir.1991), and a managing partner is a fiduciary of the limited partners, corresponding to shareholders of a corporation, although again there is no trust in the conventional sense. . . . To complicate the picture further, the cases are divided over the question whether a statute that, as in our case, deems a debtor a fiduciary in order to enlarge the remedies for default makes the debtor a "fiduciary" for purposes of section 523(a)(4).
>
> . . .
>
> The key to knitting the cases into a harmonious whole is the distinction stressed in *Davis* and other cases between a trust or other fiduciary relation that has an existence independent of the debtor's wrong and a trust or other fiduciary relation that has no existence before the wrong is committed. A lawyer's fiduciary duty to his client, or a director's duty to his corporation's shareholders, pre-exists any breach of that duty, while in the case

of a constructive or resulting trust there is no fiduciary duty until a wrong is committed. The intermediate case, but closer we think to the constructive or resulting trust pole, is that of a trust that has a purely nominal existence until the wrong is committed. Technically, Marchiando became a trustee as soon as she received her license to sell lottery tickets. Realistically, the trust did not begin until she failed to remit ticket receipts. For until then she had no duties of a fiduciary character toward the Department of Lottery or anything or anyone else. Until then, she was just a ticket agent. The state, afraid that she might be a disloyal agent, required her to keep the proceeds of her ticket sales separate from her other funds and threatened her with criminal punishment if she did not. These were devices by which the state sought to establish and enforce a lien in the proceeds, the better to collect them securely. The analogy is to "floor planning," where a bank insists that the proceeds of any sale from inventory be remitted to the bank to pay down the principal of the loan as soon as the sale is made. Such arrangements, held not to come within the scope of section 523(a)(4) in *Davis* and *Long,* are remote from the conventional trust or fiduciary setting, in which someone-a lawyer for example, or a guardian, or a managing partner-in whom confidence is reposed is entrusted with another person's money for safekeeping. See also *In re Iowa R.R.,* 840 F.2d 535, 541-45 (7th Cir.1988).

If we probe more deeply the distinction between the fiduciary relation that imposes real duties in advance of the breach and the fiduciary relation that does not we find that the first group of cases involve a difference in knowledge or power between fiduciary and principal which, as we put it in *Maksym v. Loesch, supra,* 937 F.2d at 1242, gives the former a position of ascendancy over the latter. See also *Kham & Nate's Shoes No. 2, Inc. v. First Bank,* 908 F.2d 1351, 1357 (7th Cir.1990); *Weinberger v. Kendrick,* 698 F.2d 61, 78-79 (2d Cir.1982) (Friendly, J.); *Gratz v. Claughton,* 187 F.2d 46, 49 (2d Cir.1951) (L. Hand, J.). The fiduciary may know much more by reason of professional status, or the relation may be one that requires the principal to repose a special confidence in the fiduciary; both factors are present in the case of a lawyer-client relation and also the relation between director and shareholder or managing partner and limited partner. Or the principal may be a child, lacking not only knowledge but also the power to act upon it. These are all situations in which one party to the relation is incapable of monitoring the other's performance of his undertaking, and therefore the law does not treat the relation as a relation at arm's length between equals.

All the cases except *Quaif* and *Carey* that have held debts nondischargeable by virtue of section 523(a)(4) have involved either express trusts of a conventional variety or fiduciary relations

> of the kind just described-relations of inequality that justify the imposition on the fiduciary of a special duty, basically to treat his principal's affairs with all the solicitude that he would accord to his own affairs. Nothing of the sort is involved here. The fiduciary is a ticket agent with no edge based on the possession of power or expertise; the principal is the state itself. The inequality of relation that calls for the imposition of fiduciary duties is wholly absent.
>
> If, contrary to our decision in *Judd v. First Federal Savings & Loan Ass'n,* 710 F.2d 1237, 1241 (7th Cir.1983), which holds that the word "trust" in an instrument does not by itself "transform a traditional debtor-creditor relationship into a fiduciary relationship," a fiduciary is anyone whom a state calls a fiduciary-the only principle on which the discharge of Marchiando's debt could be refused-states will have it in their power to deny a fresh start to their debtors by declaring all contractual relations fiduciary. They are not apt to go that far. They are apt to seek a preferred position for their own debts by declaring people who do business with the state fiduciaries of the state or its agencies. Illinois has tried to do this with its ticket agents. If it succeeds, next it can do it with all its other contractors. Libertarians may smile approvingly at the state's equating its bureaucracies to the children and other incompetents who are the classic trust beneficiaries, but we do not think Congress would. The convenience-store keeper who commingles the proceeds of her lottery ticket sales with her other receipts is at a considerable remove from the lawyer who converts money in his clients' escrow accounts or the bank trust department that invests someone's retirement fund recklessly.
>
> 13 F.3d at 1115-1117

The teaching of *Marchiando* is not principally that a statutory or contractual designation of an individual as a "trustee" or "fiduciary" has no real relevance to the determination of "fiduciary capacity" under § 523(a)(4). The primary lesson to be learned from the case is that there must be a "res" in existence before or at the time the designated "fiduciary" relationship truly arises. In this case, the only "res" there is arose only when Price did not make payments to Regency after her receipt of the insurance check. Price could have paid Regency with other funds, either before or after her receipt of the check, in which event the check would have been hers to cash and keep. The arrangement created contractually between Price and Regency is essentially indistinguishable from the arrangement created statutorily between the State of

Illinois and Marchiando, and just as was true in the latter, in the former there was no "fiduciary" relationship cognizable under 11 U.S.C. § 523(a)(4).

Although the Lake Superior Court held that the money at issue was held in trust by the defendant for the benefit of Regency, this is not the type of relationship which is contemplated to be within the reach of § 523(a)(4).[7] Clearly this case is akin to *Marchiando*. The purported "trust" did not begin until Price received the money and failed to turn it over to Regency. This Court has no qualms concluding that the document entitled Conditions of Admission to Regency Hospital (attached to Defendant's Response as Exhibit 'A') is not a trust agreement. Instead, it is exactly what it says it is – an assignment and guarantee to pay. The record of the state court proceeding does not support a finding that the requisite fiduciary relationship was created, and as a result Regency's argument fails under this prong of § 523(a)(4).

2. Embezzlement

Regency also asserts that the foregoing debt is excepted from discharge under § 523(a)(4)'s "embezzlement" prong. For the purpose of determining dischargeability, embezzlement and larceny are defined by federal common law. *Valentine v. Valentine*, 104 B.R. 67, 70 (Bankr. S.D.Ind. 1988). Embezzlement, under § 523(a)(4), is defined as the fraudulent appropriation of the creditor's property by the debtor to whom it has been entrusted or into whose hands it has lawfully come. *Dobek v. Dobek*, 278 B.R. 496, 509 (Bankr. N.D.Ill. 2002) (citing, *Pierce v. Pyritz*, 200 B.R. 203, 205 (Bankr. N.D.Ill. 1996); *see also, Matter of Weber*, 892 F.2d 534, 538 (7th Cir. 1989)). On the other hand, larceny is where the original taking of the property was not lawful. *Id*. at 509-10. Embezzlement differs from larceny only in

[7] Any finding of fact by the state court to the effect that Price was a fiduciary for Regency is not binding on the federal question of the elements necessary to establish a fiduciary relationship under 11 U.S.C. § 523(a)(4). The Court should also state that even if an enterprising health care provider would insert some "fiduciary"-like language into an assignment document or patient contract, the arrangement still would not fall within the ambit of § 523(a)(4).

that the original taking was lawful. *In re Rose*, 934 F.2d 901, 903 (7th Cir. 1991). As a result, by definition, before a creditor can make a claim of nondischargeability for embezzlement or larceny, it must show that the property allegedly obtained by Price through embezzlement/ larceny was property of the creditor. *Dobek*, 278 B.R. at 509-10. Contrary to the assertion of Price, establishing a *prima facie* case under § 523(a)(4) for embezzlement or larceny does **not** require a finding that a fiduciary relationship existed between Regency and Price. Rather, the finding of a fiduciary relationship is only required when attempting to demonstrate that a debt is excepted from discharge for fraud or defalcation while acting in a fiduciary capacity.

There is no question here that the funds alleged to have been misappropriated were Regency's property; the state court so determined specifically. The facts determined by the state court establish the base concept of embezzlement, as opposed to larceny: Price did initially come into possession of this money *lawfully*.

The elements of "embezzlement" under 11 U.S.C. § 523(a)(4) have been well-defined by the United States Court of Appeals in *In re Weber*, 892 F.2d 534, 538-9 (7th Cir. 1989) as follows:

> Section 523(a)(4) of the bankruptcy code does not allow a debtor to discharge a debt incurred as a result of the debtor's embezzlement. Bankruptcy courts define embezzlement as the "fraudulent appropriation of property by a person to whom such property has been entrusted or into whose hands it has lawfully come." *Moore v. United States*, 160 U.S. 268, 269, 16 S.Ct. 294, 295, 40 L.Ed. 422 (1895), *quoted in In re Bevilacqua,* 53 B.R. 331, 333 (Bankr.S.D.N.Y.1985), *In re Myers,* 52 B.R. 901, 905 (Bankr.E.D.Va.1985), *In re Graziano,* 35 B.R. 589, 594 (Bankr.E.D.N.Y.1983); *see also In re Belfry,* 862 F.2d 661, 662 (8th Cir.1988). To prove embezzlement, the creditor must show by clear and convincing evidence that (1) the debtor appropriated funds for his or her own benefit; and (2) the debtor did so with fraudulent intent or deceit. *In re Taylor,* 58 B.R. 849, 855 (Bankr.E.D.Va.1986); *In re James,* 42 B.R. 265, 267 (Bankr.W.D.Ky.1984); *In re Storms,* 28 B.R. 761, 765 (Bankr.E.D.N.C.1983); *Graziano,* 35 B.R. at 595.
>
> Ablan initially argues that the bankruptcy court should have

> applied the embezzlement and conversion laws of Wisconsin. Although he cites no authority for this proposition, and admits that ultimately the issue of nondischargeability is a question of federal law, he claims that state law is "useful" in defining the elements of embezzlement. Ablan claims that the Wisconsin cases he cites "do not in any event conflict with the [federal standards]"; his analysis of this case law, however, leads him to conclude that "[t]he act of depositing [another's] funds into one's account, thereafter causing them ··· to be dispersed for one's own purposes or uses is the kind of evidence which *would compel the conclusion that embezzlement has occurred.*" (emphasis added). Under federal law, such a conclusion is not compelled since the creditor must also prove that the dispersal occurred with fraudulent intent. Thus, Ablan had to prove more than just the fact that Weber used the sales proceeds to pay off his personal debts; he had to prove that Weber did so with fraudulent intent.

The element of fraudulent intent is a constant in federal decisions under § 523(a)(4)'s "embezzlement" and "larceny" prongs; See, e.g., *In re Dempster*, 182 B.R. 790, 802 (Bankr. N.D.Ill. 1995); *In re Fields*, 2005 WL 2205787 (Bankr. C.D.Ill. 2005); *In re Brady*, 101 F.3d 1165, 1172-3 (6th Cir. 1996); *In re Rogstad,* 126 F.3d 1224, 1228 (9th Cir. 1997); *In re Fuget*, 339 B.R. 702, 707 (Bankr. S.D.Iowa 2006); *In re Lammers*, 2005 WL 1498336 (Bankr. M.D.Fla. 2005). In order to sustain an action for "embezzlement" or "larceny" under 11 U.S.C. § 523(a)(4), the plaintiff must established not only that the debtor exercised unauthorized control over property, but that the debtor had a fraudulent intent in doing so.

The issue then becomes whether collateral estoppel applies to the matter now before this Court under § 523(a)(4)'s embezzlement prong. In order to satisfy the first and third elements of estoppel, which are somewhat intertwined, this Court must find that the issues, which are necessary for finding an exception to discharge under § 523(a)(4), were presented to and involved in the state court action and that they were necessary to the state court's determination of liability. These issues include whether the property was that of the creditor; whether the property was either entrusted to debtor or that came into her hands lawfully; and whether it was fraudulently appropriated.

First, the Court will look at the issue of "appropriation of the creditor's property". The state court's decision determined that Price committed conversion, not embezzlement. The place to start is thus to analyze the elements for conversion under Indiana law. Indiana Code 35-43-4-3 provides in pertinent part:

> a) A person who knowingly or intentionally exerts unauthorized control over property of another person commits criminal conversion, a Class A misdemeanor.
>
> *See*, I.C. 35-43-4-3(a) (West 2006).

Indiana Code 35-43-4-1 defines the "exertion of control over property" and "unauthorized" as follows:

> (a) As used in this chapter, "exert control over property" means to obtain, take, carry, drive, lead away, conceal, abandon, sell, convey, encumber, or possess property, or to secure, transfer, or extend a right to property.
>
> (b) Under this chapter, a person's control over property of another person is "unauthorized" if it is exerted:
>
> (1) Without the other person's consent;
>
> I.C. 35-43-4-1(a) &(b) (West 2006).

The critical element of the tort of conversion under Indiana law is the exercise of unauthorized control over the property of another: "To constitute the tort of conversion, there must be an appropriation of the property of another;" *Stevens v. Butler*, Ind. App., 639 N.E.2d 662, 666 (1994). As stated in *Indiana & Michigan Electric Company v. Terre Haute Industries, Inc.*, Ind. App., 507 N.E.2d 588, 610 (1987):

> Conversion is a tort involving the appropriation of personal property of another to the tortfeasor's own use and benefit, to the exclusion of and in defiance of the owner's rights, under an inconsistent claim of title; mens rea is not an essential element. 6 I.L.E. *Conversion* sec. 11 (1958). Thus, the mere existence of the tort does not necessarily carry with it the imputations of malice, so even if the tortfeasor acted in good faith in assuming dominion over the property, such is no defense. *Howard Dodge & Sons, Inc. v. Finn* (1979), 181 Ind.App. 209, 391 N.E.2d 638. Lack of consent by the owner is an element. 6 I.L.E. *Conversion* sec. 13 (1958).

As to conversion, the state court specifically found that ". . . Sandra Price intentionally acted dishonestly with the intent to exercise unauthorized control over the funds paid by Anthem which belonged to and were the property of Regency by reason of the assignment of benefits provision approved by her." (emphasis supplied) See, *Findings and Judgment* at page 8. The state court also specifically determined that Price had converted Regency's property. This is as close to "appropriation of the creditor's property" under the embezzlement prong of § 523(a)(4) as one can get. Therefore, this issue was clearly involved in the state court proceeding and these findings were obviously necessary for the finding of liability for conversion against the defendant.

Now for the issue of whether the property was fraudulently appropriated. Regency, in its state court complaint, specifically pled a separate count to recover a number of fraudulent transfers. Based upon the finding of the Lake Superior Court, fraudulent intent was clearly an issue in that case. As the Court found:

> The Court finds that all of the transfers of funds to the Defendants and other friends of Sandra Price were made gratuitously, without consideration being exchanged, and that the transfers were made by Sandra Price with the specific intention of hindering payment, defrauding Regency, or otherwise making the funds unavailable to Regency for the payment on the account of Clarence Price. (emphasis supplied)

See, *Findings and Judgment,* pgs. 6-7

Also, for estoppel purposes, these findings were without question necessary to the state court proceeding. Under Indiana law, for this type of cause of action, intent is a vital element:

> A transfer made or an obligation incurred by a debtor is fraudulent as to a creditor, whether the creditor's claim arose before or after the transfer was made or the obligation was incurred, if the debtor made the transfer or incurred the obligation:
>
> (1) with actual intent to hinder, delay, or defraud any creditor of the debtor; or
>
> (2) without receiving a reasonably equivalent value in exchange for the transfer or obligation, and the debtor:
>
> (A) was engaged or was about to engage in a business or a

> transaction for which the remaining assets of the debtor were unreasonably small in relation to the business or transaction; or
>
> (B) intended to incur or believed or reasonably should have believed that the debtor would incur debts beyond the debtor's ability to pay as the debts became due.
>
> I.C. 32-18-2-14

Indiana courts have held that this intent to defraud can be inferred through various "badges of fraud":

> 1. transfer of property by a debtor during the pendency of a suit;
> 2. transfer of property that renders the debtor insolvent or greatly reduces his estate;
> 3. a series of contemporaneous transactions which strip a debtor of all property available for execution;
> 4. secret or hurried transactions not in the usual mode of doing business;
> 5. any transaction conducted in a manner differing from customary methods;
> 6. a transaction whereby the debtor retains benefits over the transferred property;
> 7. little or no consideration in return for the transfer; and
> 8. a transfer of property between family members.
>
> *Commercial Credit Counseling Services, Inc. v. W.W. Grainger, Inc.,* 840 N.E.2d 843, 852 (Ind. App. 2006)

The state court found that a number of these "fraud indicators" existed at the time Price transferred the money. The facts adduced by the state court clearly support the foregoing conclusion. Instead of forwarding the money she received to Regency, Price proceeded to purchase luxury items such as new furniture and a new car. She issued several bank drafts, most in the amount of $5,000.00, and disbursed them to friends and family in four different states; not to mention the fact that she set up three different bank accounts, which were attached by Regency in the state court proceeding. She did not remit any of the money she received from Anthem to Regency. The court found that these transfers to several family members and friends were with no consideration being exchanged and, as a result, the debtor intentionally rendered herself virtually judgment proof. Clearly, these findings are necessary to the state court's decision and, more importantly, provide this Court with the requisite fraudulent

intent necessary to establish and prove an action for embezzlement under § 523(a)(4).

Finally, the issue of Price's lawful receipt of the subject funds was an issue which was involved in the state court action. The record demonstrates that the funds were received by Price pursuant to the assignment provision of the Conditions of Admission: "The Court finds that Regency requested Sandra Price to approve the conditions of admission, that she did in fact approve the conditions of admission. . ." and "Anthem reviewed the billing, approved it, and on or about October 4, 2004, issued a benefit check for payment on the medical expenses in the sum of $302,086.63, which check was made payable to Sandra Price and forwarded directly to her." See, *Findings and Judgment,* pg. 3. This was necessary to the state court proceeding in that it established that Price had actually received the money to which she exercised the unauthorized control.

Thus, the issue of fraudulent misappropriation of Regency's funds by Price was both litigated in the state court, and was necessary to that court's judgment.

Finally, Price was represented at the trial, and had full opportunity to present her case. Price's "defense" to Regency's motion for summary judgment is essentially that proceedings in the state court were unfair from their inception. However, the fact of the matter is that this is not a state appellate court. Many of the issues raised by Price in this proceeding are either a direct attack, or a back door attack, on the validity of a judgment to which this Court must give full faith and credit.

Therefore, the foregoing issues adjudicated in the state court action are given preclusive effect in the current proceeding and likewise establish that Regency's debt is excepted from discharge pursuant to § 523(a)(4) for embezzlement.

The Supreme Court of the United States has held that the phrase "debt for" in § 523(a)(4), and throughout § 523(a) generally means "debt as a result of", "debt with respect to", and "debt by reason of". *Cohen v. De La Cruz*, 523 U.S. 213, 220 (1998). Consequently,

the term "debt" includes exemplary damages, attorney's fees and other relief which may exceed the debt itself, when the state law allows these "tag on" damages as a recovery for a debt excepted from discharge under federal law. See, *Id.* at 223. As the Court opined:

> Limiting the exception to the value of the money or property fraudulently obtained by the debtor could prevent even a compensatory recovery for losses occasioned by fraud. For instance, if a debtor fraudulently represents that he will use a certain grade of shingles to roof a house and is paid accordingly, the cost of repairing any resulting water damage to the house could far exceed the payment to the debtor to install the shingles. See *In re Church*, 69 B.R. 425, 427 (Bkrtcy. Ct. ND Tex. 1987).
>
> *Id.* at 222.

As a result, the entire debt, including exemplary damages and attorneys' fees, in the amount of $318,797.05 ($403,047.67 less credits of $84,205.62,), is excepted from discharge.

B. 11 U.S.C. § 523(a)(6)

Regency also posits the argument that this debt is excepted from discharge under § 523(a)(6). 11 U.S.C. § 523(a)(6) in pertinent part states:

> **(a)** A discharge under section 727 . . . of this title does not discharge an individual debtor from any debt–
>
> . . .
>
> **(6)** for willful and malicious injury by the debtor to another entity or to the property of another entity.

In *In re Whiters*, 337 B.R. 326 (Bankr. N.D.Ind. 2006), this Court determined that in order to sustain an action under 11 U.S.C. § 523(a)(6), a creditor must demonstrate the following:

1. The Debtor's actions caused an "injury" to the person or property interest of the creditor.
2. That the debtor's actions which caused the injury were the result of "willful" conduct by the debtor by which the debtor intended to effect an injury to the person or property interest of the creditor.
3. That the debtor's "willful" acts were undertaken in a "malicious" manner.

As this Court recognized then, it is difficult to establish the foregoing in a default judgment or summary judgment type of proceeding. Some courts developed a standard, which

was rejected in *Whiters*, that the "willful" element may be established by either proof that there was an "objective substantial certainty of harm", or a "subjective motive to do harm". It is this Court's view that the "willful" element all depends upon the defendant's/debtor's subjective state of mind. As the Sixth Circuit stated in the matter of *In re Markowitz,* 190 F.3d 455, 464 (6th Cir. 1999):

> The Court's citation to the Restatement's definition of "intentional torts" underscores the close relationship between the Restatement's definition of those torts and the definition of "willful and malicious injury." The Restatement defines intentional torts as those motivated by a desire to inflict injury or those substantially certain to result in injury. Although the Supreme Court identified a logical association between intentional torts and the requirements of § 523(a)(6), it neither expressly adopted nor quoted that portion of the Restatement discussing "substantially certain" consequences. Nonetheless, from the Court's language and analysis in *Geiger,* we now hold that unless "the actor desires to cause consequences of his act, or . . . believes that the consequences are substantially certain to result from it," Restatement (Second) of Torts § 8A, at 15 (1964), he has not committed a "willful and malicious injury" as defined under § 523(a)(6).

The "malicious" element has been defined by the Seventh Circuit as, "[The] conscious disregard of one's duties or without just cause or excuse; it does not require ill-will or specific intent to do harm." See, *in re Thirtyacre*, 36 F.3d 697, 700 (7th Cir. 1994). However, a unique set of problems arise in the context of a conversion action as recognized in *Avco Financial Services of Billings v. Kidd (In re Kidd),* 219 B.R. 278 (Bankr.D.Mont.1998):

> The problem with conversion cases . . . is that rarely are the debtors acting out of a desire to injure the creditors, even though the injury to the creditor, although not desired, is almost always substantially certain to result from a debtor's actions. Thus, the key in conversion cases is to analyze each set of circumstances on a case-by-case basis to determine whether the conversion is in the nature of an intentional tort or whether the conversion is a result of a negligent or reckless tort – but not willful or malicious.

In the *Whiters* opinion, this Court wrestled with this issue in great detail:

> In light of *Geiger,* the standard for willful under § 523(a)(6) appears to be the same for conversion as for any other injury: to be willful, the debtor must intend that conversion of the collateral injure the creditor or the creditor's lien interest. However, *Geiger* does not address the evidence by which intent to injure can be established. We believe that as to proof of intent to injure in the context of conversion of secured property, *Posta* and *Pasek* remain instructive. Intent may be established by either direct or indirect evidence. *Posta,* 866 F.2d at 367. Willful injury may be established by direct evidence of specific intent to harm a creditor or the creditor's property. *Id.* Willful injury may also be established indirectly by evidence of both the debtor's knowledge of the creditor's lien rights and the debtor's knowledge that the conduct will cause particularized injury. *In re Pasek,* 983 F.2d 1524 at 1527 (1993). *See also* RESTATEMENT (SECOND) OF TORTS § 8A (1965) ("The word 'intent' is used throughout the Restatement of this Subject to denote that the actor desires to cause consequences of his act, or that he believes that the consequences are substantially certain to result from it.").
>
> In re Whiters, 326 B.R. at 346-50

The subject funds were in fact the property of Regency.[8] Obviously, for estoppel purposes, this particular issue is identical to that confronted by the state court in deciding whether Price committed the tort of conversion (i.e., unauthorized control over the property of another). With that established, what of the "willful" and "malicious" requirements in light of *Geiger* and *Whiters*?

In a conversion case, the key element of "intentional" injury is not whether the debtor intended to harm the creditor as an economic entity, but rather whether the debtor intended to injuriously impact the creditor's property interest. That property interest was the utilization of the insurance proceeds which Price, after having assigned them to Regency, received, to compensate Regency for the services it provided to Mr. Price. The facts established by the state court demonstrate that Price intentionally took money – earmarked explicitly for her

[8] The state court specifically found that ". . . Sandra Price intentionally acted dishonestly with the intent to exercise unauthorized control over the funds paid by Anthem which belonged to and were the property of Regency by reason of the assignment of benefits provision approved by her." See, *Findings and Judgment* at page 8.

deceased husband's medical expenses – bought herself luxury items, and disbursed bank drafts to so many people in four different states that any attempt to retrieve it would be impractical, if not impossible. She left herself with scant funds to repay the debt owed to Regency. The state court record establishes the requisite subjective intent to harm Regency's interests in the proceeds of the insurance payment.

As shown by the record, Price has yet to climb to the mountain top and exclaim, "I intended harm to the property of Regency!!". In order to reach this conclusion, the inquiry is not whether Price intended Regency to go unpaid, but whether she intended to use the creditor's money for a purpose other than for payment of its debt. This is the same issue confronted by the state court and was necessary in determining that certain "badges of fraud" existed – namely Price intentionally rendering herself judgment proof so that no property would be available for Regency to execute upon in satisfaction of its debt; which coincidentally demonstrated fraudulent intent on the part of the debtor.

In this case, given the facts determined by the state court, there can be no other reasonable conclusion than that it was the debtor's intent to use Regency's money for something other than payment of its debt. This money, in varying amounts, was transferred to twenty-two different people – mostly family and friends. The debtor purchased herself furniture, carpeting, and a new car. All the while, even after the state court action was filed, she made no attempt to use this money to pay Regency's debt. Instead the creditor was required to seek an injunction from the state court freezing these accounts and seizing the car. As a result, there was an intentional injury, and Price's actions in this regard were willful.

To satisfy the "malicious" requirement of § 523(a)(6), there must be a conscious disregard of one's duties without just cause or excuse, i.e. knowledge of wrongdoing. For estoppel purposes, this was an issue confronted by the state court and was necessary in

finding that there was intent to fraudulently transfer Regency's money. In the state court action, the court closely examined Price's actions in relation to Regency's property and found that the transfers of money were done, "gratuitously, without consideration being exchanged, and that the transfers were made by Sandra Price with the specific intention of hindering payment, defrauding Regency, or otherwise making the funds unavailable to Regency for the payment on the account of Clarence Price." In support of this, the court found that upon receiving the money, Price consulted attorney George Paras who advised her that Regency was entitled to every dime. The court also found that numerous phone calls were made, and that a letter was sent "return receipt", to the debtor reminding her of the assignment. So what did the debtor do? She proceeded to purchase luxury items, issued several bank drafts in small denominations and disbursed them to friends and family in four different states, and set up three different bank accounts – one with her brother. She was told outright by an officer of the court that it was **wrong** to keep the money. As the state court found, Price, "deliberately rendered herself judgment-proof so that there would be few, if any, funds available to pay Regency". This is as "knowingly wrong" as it gets. The foregoing findings were necessary for a finding of fraudulent intent and, consequently, this Court concludes that the actions of Sandra Price were also 'malicious' within the meaning of § 523(a)(6).

Finally, for the final two estoppel requirements as to issues involving "wilful" and "malicious", the Court also finds that for the reasons stated *supra*, these matters were fully litigated in the state court and Price was fully represented by counsel.

Price's indebtedness to Regency, as determined by the Lake County, Indiana, Superior Court, is excepted from discharge under 11 U.S.C. §523(a)(6).

V. Conclusion

The foregoing issues adjudicated in the state court action are given preclusive effect in

the current proceeding. There is no genuine issue as to any material fact, and Regency is entitled to judgment as a matter of law, and that Regency's entire debt, including exemplary damages and attorneys' fees,[9] in the amount of $318,797.05 ($403,047.67 less credits of $84,205.62,) is excepted from discharge pursuant to 11 U.S.C. § 523(a)(4) and 11 U.S.C. § 523(a)(6).

IT IS THEREFORE ORDERED, ADJUDGED AND DECREED that Regency Hospital of Northwest Indiana, LLC is entitled to summary judgment on its claims asserted in the adversary proceeding.

IT IS FURTHER ORDERED, ADJUDGED AND DECREED the Lake County Superior Court's judgment in case number 45D11-0503-PL-18, and the findings of facts and conclusions of law stated therein, is entitled to be given preclusive effect under the doctrine of collateral estoppel as to the action filed by the plaintiff in this Court under Case No. 05-6181, and that the judgment rendered in that action in the amount of $318,797.05 is excepted from discharge under 11 U.S.C. § 523(a)(4) and 11 U.S.C. § 523(a)(6) .

Dated at Hammond, Indiana on December 7, 2006.

/s/ J. Philip Klingeberger
J. Philip Klingeberger
United States Bankruptcy Court

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Attorneys of Record

[9] See *supra* for a discussion of *Cohen v. De La Cruz*, 523 U.S. 213, 220 (1998), concerning the award of attorneys' fees and costs.